

Service Date: December 7, 1984

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER of the Application)	UTILITY DIVISION
of the City of Belgrade to Increase)	DOCKET NO. 84.6.27
Rates and Charges for Water Service)	ORDER NO. 5100

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FINAL ORDER

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APPEARANCES

FOR THE APPLICANT:

William A. Schreiber, City Attorney, City Hall, Belgrade,
Montana 59714

FOR THE INTERVENORS:

John Allen, Staff Attorney, Montana Consumer Counsel, 34 West
6th Avenue, Helena, Montana 59620

FOR THE COMMISSION:

Opal Winebrenner, Staff Attorney, 2701 Prospect Avenue, Helena,
Montana 59620

BEFORE:

Clyde Jarvis, Commissioner and Hearing Examiner

BACKGROUND

1. On June 13, 1984, the City of Belgrade (Applicant or City) filed an application with this Commission for authorization to increase rates and charges for water service to its customers in the Belgrade, Montana area. The Applicant requested an average increase of approximately 42% which would result in an annual revenue increase of approximately \$71,000.

2. On September 13, 1984, pursuant to notice of public hearing, a hearing was held in the City Council Chambers, City Hall, Belgrade, Montana. The purpose of the public hearing was to consider the merits of the Applicant's proposed water rate adjustment. At the close of the public hearing, the parties stipulated to allow the Commission to issue a Final Order in this Docket.

FINDINGS OF FACT

3. At the public hearing, the Applicant presented the testimony and exhibits of:

Thomas Jack Lunt, Mayor

Kelley Reimche, City Clerk/Treasurer

Henry Hathaway, City Water Superintendent

Tom McIsaac, Fire Chief

Doug Daniels, Consulting Engineer/City Engineer

Tom, Consulting Engineer

These witnesses testified relative to: the need for proposed capital improvements, the estimated cost of proposed capital improvements, the financing of proposed capital improvements, current and projected debt service obligations of the water utility, the financial condition of the water utility, fire flow problems and rate structure.

4. No public testimony was presented at the public hearing in opposition to any issue under consideration by the Commission in this Docket.

Proposed Capital Improvements

5. The City, in its application, has proposed a capital improvement program which includes the development of water wells to increase available water supply, the construct on and/or replacement of distribution and transmission mains to improve water flows, the purchase of leak detection equipment, the establishment of a construction fund for water main repair or replacement where major leaks or numerous leaks are detected and the purchase of water meters. The City proposes that the capital improvement program under consideration in this Docket be funded through the execution of a loan agreement with the Montana Department of Natural Resources, which is administering a funding program passed by the 1983 Montana Legislature.

6. The City's proposed capital improvement program provides for the looping of the 6 inch mains along Texas Street and in Rosebud, Cascade, Custer and Jefferson Avenues at an estimated cost of \$40,900. The City's witnesses indicated that the looping in this area would improve distribution pressures and eliminate the potential health hazard attendant with dead-end mains.

7. The City proposes, in its capital improvement program to replace the 1 inch line in Nevada Street between Madison and Jefferson Avenues and replace the 4 inch line on Jefferson Avenue from Nevada to Texas Street with a 10 inch water main, estimating the cost at \$37,200. The City's consulting engineers stated that the lines presently in place in these areas were of inadequate size causing inadequate pressures to be experienced by consumers located in the area.

8. The capital improvement program also includes the

construction of a 6 inch main within the street right-of-way on Minnesota Street between Jefferson ' and Cascade Avenues, replacing a currently existing 4 inch main, that is not constructed within the right-of-way, at an estimated cost of \$13,400. The fact that the existing main is not located in the right-of-way presents a problem for the City, in that, if repairs to the main are needed the City must obtain permission from the land owner before commencing any repairs. The City also indicated that the main was of insufficient size and caused restrictions in the flow.

9. Another improvement proposed by the City is the extension of an 8 inch water main from the existing 10 inch main adjacent to U.S. Highway No. 10, south across the railroad tracks, and along Oregon Street to Yellowstone Avenue. This line will replace an old 6 inch steel line under the railroad tracks, which is in poor condition, and an existing 4 inch line on Oregon Street between Silver Bow and Yellowstone Avenue and will cost approximately \$94,400.

10. The proposed capital improvement program provides for the construction of an 8 inch water main on Madison Avenue from Oregon Street to Colorado Street, and a 10 inch water main from Colorado to Nevada Street. This will replace a portion of the existing 4 inch and 6 inch pipe on Madison Avenue, between Minnesota and Nevada Streets. The City anticipates that construction of this line will increase flows in the area and replace some existing pipe that is in poor condition, at an estimated cost of \$104,500.

11. The last distribution system improvement outlined by the City is the construction of a 10 inch water main from the well on Broadway Street to the intersection of Broadway and Madison Avenue. This 10 inch main will be connected with the 10 inch

mains proposed to be constructed on Madison Avenue Nevada Street and Jefferson Avenue The City explained that construction of the 10 inch main on Broadway was necessary to improve water flows to consumers connected to the service in that area and that the cost of this improvement was approximately \$27,300.

12. Included in the capital improvement program funding is a request for authorization to purchase approximately \$6,000 worth of water meters. The City stated that it has been receiving an increasing number of requests from consumers for water meters and that it wanted a stock of meters on hand to provide consumers when requests were made.

13. Some of the City witnesses indicated that the water utility operation was experiencing an excessive amount of lost and unaccounted for water, that a major contributing factor to losses are leaks in the transmission and distribution system. The City Water Superintendent, Mr. Hathaway, testified that during the summer of 1984, the City had located 20 leaks on the system and the water department only had sufficient funds available to repair 2 of the leaks located.

Because the City's operating personnel have indicated that leaks are a significant contributing factor to the water utility's lost and unaccounted for water problem, the City has included in its capital improvement program the cost of leak detection equipment and establishment of a construction fund for water main repair or replacement, estimating the cost at \$90,000.

14. Well No. 3, completed in October, 1981, has been the subject of litigation between the City and the contractor that drilled the well, since its completion. Apparently that

litigation is ending and the City will have this well available to increase its source of supply which is alleged inadequate during peak demand periods.

The City, in its proposed capital improvement program, has included an estimate cost of \$115,000 to bring this well on line. The estimated cost includes the purchase and installation of a pump, piping and controls to operate the well, and also the construction of a well house.

15. The need for the proposed capital improvement program outlined by the City was not challenged by any party participating in this proceeding. The Commission, having considered the testimony of the City that problems are being experienced by consumers of the water utility service, the indication that water flows in certain areas of the City are inadequate, that the available source of water supply is inadequate during periods of peak demand, that leaks in the transmission and distribution system are major contributing factors to the City's lost and unaccounted for water, and that some of the mains being replaced are in an advanced stage of deterioration, finds that it is prudent for the City to construct the proposed capital improvements to correct these deficiencies.

The Commission also finds the City's estimated cost of \$528,700 for constructing the improvements outlined in Findings of Fact Nos. 6 through 14 to be a reasonable estimate.

Capital Improvement Refinancing

16. The City, in its loan application to DNRC, included the refinancing of \$252,000. The City, at the present time, has an

outstanding loan with Valley Bank in the amount of \$252,000, the proceeds of which are being used for the construction of a well and associated facilities.

The City expressed a desire to include the construction costs for the well and associated facilities in its loan transaction with DNRC, because the interest rate available from DNRC's lower than the interest rate currently applicable to the Valley Bank loan. The Commission finds the City's request to refinance the outstanding loan to be reasonable, because the lower interest rate available from DNRC will result in a lowering of the overall cost of providing service.

Miscellaneous Costs Associated With Capital Improvements

17. The Applicant has included ancillary costs associated with its capital improvement program such as Engineering, Legal and Administrative, funding a portion of the Bond Reserve and DNRC Administration. The total estimated cost for these items is \$159,300. These miscellaneous costs are typically incurred during a major construction program and appear to be reasonable.

18. The Commission, based on Findings of Fact Nos. 15, 16 and 17, finds the estimated cost of capital improvements to be financed, under consideration in this Docket, to be \$940,000.

Debt Service

19. The City proposes to finance the capital improvement program outlined in the preceding Findings of Fact through the issuance of revenue bonds with the purchaser of the bonds being the Montana Department of Natural Resources and Conservation

(DNRC).

The City is proposing the issuance of \$940,000 in revenue bonds to be repaid over a period of 20 years with an interest rate of 7% during the first 5 years, and 10.26% for the remaining 15 years. Under this financing, the City proposes a bond reserve in an amount equal to the maximum principal and interest payment on the bonds and provide a debt service coverage of 125%.

20. The City has a current outstanding water revenue bond payable to the Farmers Home Administration with an annual principal and interest payment of approximately \$48,700 and a present coverage ratio requirement of 110%. The City does not anticipate retiring this bond issue with the issuance of the proposed revenue bond issue. Therefore, the City will be incurring bond payments that are additional to those just described.

21. Since the City will not be retiring the bond issue payable to the Farmers Home Administration it will have to comply with the requirements outlined in Resolution No. 454, Section 10, regarding the issuance of additional revenue bonds on parity with the current outstanding issue. Section 10 provides in part that parity issue, must provide for a bond reserve account in an amount equal to one year's debt service on the respective additional bond issue. The City must also provide debt service coverage of 120% for all outstanding bonds.

It is the Commission's understanding that if a City has a currently outstanding revenue bond issue, DNRC adopts the provisions of that bond indenture for purposes of establishing revenue bond reserve requirements and debt service coverage. Since the requirements of DNRC's bond indenture will not exceed

those contained in the current indenture, the Commission finds no reason to grant requirements that exceed those contained in the current indenture. The Commission finds that the establishment of a bond reserve in an amount equal to one year's principal and interest payment, and a debt service coverage of 120% to be appropriate for the DNRC bond issue.

22. The City's Exhibit No. 2 at page 1 of 2 indicates that, as of the year ending June 30, 1984 the City had a total balance in reserve funds of \$137,395. The City of Belgrade's Resolution No. 459 requires the City to maintain a fund balance of \$12,300 in its "Operating Account" and a fund balance of \$48,423 in the revenue bond Account". Therefore, the City has \$60,723 in its reserve fund that is encumbered. Reducing the total reserve fund balance by the amount of the encumbered funds, the City should have \$76,672 in its reserve funds available to reduce the amount of the proposed revenue bond issue or meet additional reserve requirements.

23. Under normal circumstances, this Commission would order that the balance of the reserve funds that are unencumbered be used to either reduce the amount of the proposed revenue bond issue or fund the additional reserve requirements resulting from the new bond issue. In this case, the Applicant has indicated that if the City should lose the litigation involving Well No. 3, approximately \$70,000 will be needed for reconstruction of the well. Well No. 3 is needed to insure an adequate supply of water to the City's consumers. Given the uncertain outcome of the litigation regarding Well No. 3, the Commission finds it appropriate to allow the City to maintain the \$76,672 in its reserves as a contingency fund for reconstruction of the well. The Commission further finds that should these unencumbered funds not be needed for the reconstruction of the well, the City should place this balance in

the "Revenue Bond Reserve" to fund the additional requirement in this account.

24. Based on the preceding Findings of Fact, the Commission finds that the Applicant should be authorized to issue \$540,000 in revenue bonds with a term of 20 years and an interest rate of 7% during the first 5 years and 10.26%, for the remaining 15 years. The Commission also finds that the bond issuance should contain the requirements that the City establish a bond reserve in an amount equal to one year's debt service on the bond and provide a debt service coverage of 120%.

25. The existing FmHA revenue bond issue has an annual principal and interest payment of approximately \$48,700. The proposed revenue bond issue will have an annual principal and interest payment of approximately \$89,000, for a total annual principal and interest payment of \$137,700. This item of expense was not challenged by any party in this proceeding, and is, accepted by the Commission.

26. The requirement that the City provide a debt service coverage of 120% means that the City must have a net operating income of \$27,540. To determine net operating income, operation and maintenance expense, as well as total debt service, are subtracted from the total revenues of the utility. The required net operating income is calculated by multiplying the annual principal and interest payment on bond issues by 20 percent ($\$137,700 \times .20 = \$27,540$)

Operation and Maintenance Expense

27. The test year in this case is the fiscal year ending June 30, 1984 adjusted for inflation. The test year operation and maintenance expenses totaling \$76,200 were not challenged by

any party participating in this proceeding, and are accepted by the Commission.

28. Based on Findings of Fact Nos. 25, 26, and 27, the Commission finds the following test year operating revenue deductions to be reasonable:

Operating Expenses	\$ 76,200
Debt Service	137,700
Coverage Ratio	<u>27,540</u>
 TOTAL	 \$241.440

Revenue Need

29. The City indicated, that under present rates, user charges would generate approximately \$168,000) in annual revenues. The test period user charge revenues, as calculated by the Applicant, appear to fairly reflect revenues that would be generated, under present rates, and are, therefore, accepted by the Commission.

30. The City's water department has source of revenue other than user charges, which include:

Sale of Material	\$ 200
Miscellaneous	2,000
Interest Earnings	8,000
TOTAL OTHER INCOME	\$10,200

The "Sale of Material and "Miscellaneous", revenue sources are based on average income received during the last five years, and were not challenged by any party participating in the hearing. The Commission accepts the projected revenue for these two accounts.

31. The interest earnings that will be received by the Applicant during the test period was the subject of

considerable cross-examination. The Applicant, for the rate case presentation, indicated that interest earnings would approximate \$8,000 annually on reserve fund investment, but actual experience for fiscal year 1984 was \$14,026. This disparity between rate case amount and actual experience brought into question the accuracy of the Applicant's projection of anticipated income from this source.

The City Clerk testified that funds were being invested at an interest rate of between 9 and 10 percent at the time of the hearing. Interest rates in the recent past have been very volatile, therefore, it is difficult to assign a fixed interest rate to funds that may be invested by the utility, and to then determine with any degree of accuracy the actual interest income that will accrue to the Applicant. The Commission is cognizant of the fact that there will be an increase in funds available to invest, and therefore is of the opinion that actual interest earning:- of \$14,025 should be substituted for the \$8,000 rate case amount presented by the Applicant. It is not logical to assume that a decrease will occur with increased funds available to invest.

29. The Commission based on Findings of Fact Nos. 29, 30, and 31, finds that the total test period operating revenues are \$184,226.

33. The Commission, based upon Findings of fact contained herein, finds that the Applicant should be allowed to increase annual revenues by \$57,214. This requirement is calculated as follows:

Operating Revenues	\$184,226
LESS:	
Operating Expenses	\$ 76,200

Debt Service	137,700
Coverage Ratio	<u>27,540</u>
Total Revenue Requirement	\$241,440
REVENUE DEFICIENCY	\$ 57,214

Rate Design

34. The Applicant's proposed rate design was not challenged by any party participating in this hearing, and is a continuation of the presently approved and effective rate structure for the City of Belgrade. The Commission's examination of the rate structure indicates that it appears to equitably distribute the cost of providing service to the various customer classifications.

35. At the public hearing, the Applicant stated that an error had been made in printing its original proposed rate structure and requested that the rate for the 1 1/4 inch meter be increased from the \$30.00 rate originally submitted to a rate of \$35.00 per month. The Commission approves this revision subject to a modification to reflect the adjusted revenue level granted herein.

Miscellaneous

36. The Commission expressed concern during the public hearing that part of the proposed system improvements, relating to increasing the source of supply and enlarging distribution mains in order to provide adequate flows in certain areas, may have been necessitated as a result of the City allowing an expansion of its service area to include subdivision developments. The Commission would advise the City that when it is considering an enlargement of its service area, it should consider whether or not an increase in its available water supply is needed to provide adequate service to the area and if

an enlargement of distribution mains will be required to insure adequate flows. If additional supply is necessary or enlargement of mains required, the City should be attributing the cost of providing these items to those consumers residing in the enlarged service area and not the general ratepayer. The enlarged service area is the identifiable source causing the increased cost and therefore, should have the responsibility to pay for the improvements rather than the general ratepayer.

CONCLUSIONS OF LAW

1. The Montana Public Service Commission properly exercises jurisdiction over the parties and subject matter in this proceeding. Title 69, Chapters 3 and 7, MCA.
2. The Commission afforded all parties notice of public hearing and an opportunity to participate in this proceeding. Section 60-3-303, MCA.
3. The rates approved herein are reasonable and just. Section 69-3-201 MCA.

ORDER

THEREFORE, THE MONTANA PUBLIC SERVICE COMMISSION ORDERS THAT:

1. The City of Belgrade shall file tariffs consistent with the Findings of Fact for Docket No. 84. 6.27 contained herein.
2. The City of Belgrade is authorized to issue a revenue bond in the amount of \$940,00 with requirements outlined in Finding of Fact No.24.
3. The City of Belgrade is authorized to file increased rates recognizing increased costs of operation and the costs associated with the proposed revenue bond issue. The rates

shall become effective upon Commission approval, subsequent to the issuance of the revenue bond.

4. The rates approved herein shall not become effective until the tariffs and the necessary calculation relating to their derivation have been submitted and approved by the Commission.

DONE IN OPEN SESSION at Helena, Montana this 3rd day of December 1984, by a vote of 5 to 0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

Clyde Jarvis, Commissioner
and Hearing Examiner

Thomas J. Schneider, Chairman

John B. Driscoll, Commissioner

Howard L. Ellis, Commissioner

Danny Oberg, Commissioner

ATTEST:

Laura Bird, Acting Secretary

Madeline L. Cottrill
Commission Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within (10) days. See 38,.2.4806, ARM.